

AR56

HANDS-ON APPROACH
MAXIMUM PROFITABILITY

1997 ANNUAL REPORT
PENN WEST PETROLEUM LTD.

Wildcat Business Reference
University of Alberta
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PENN WEST
Petroleum Ltd.

□ CORPORATE PROFILE

Penn West Petroleum Ltd. is a natural gas weighted intermediate Canadian oil and natural gas producer which is sustaining strong growth through exploration and development of internally generated prospects. Penn West exited 1997 with production of 174 mmcf/day of natural gas and 13,100 bbls/day of oil and liquids.

Penn West's hands-on team focuses on maximizing the Company's profitability by achieving cost-effective growth in production and reserves. Penn West's producing properties and large base of undeveloped land are concentrated in five Core Areas of activity in Western Canada which provide a broad range of short, medium and longer term natural gas and oil prospects.

Penn West is a publicly traded company listed on The Toronto Stock Exchange, under the trading symbol "PWT." As at March 31, 1998, there were 40,589,936 common shares issued and outstanding. Since 1995, Penn West has been part of the TSE 300 Composite Index.

□ ANNUAL GENERAL MEETING

The annual general meeting of the shareholders of Penn West Petroleum Ltd. will be held in the Belaire Room, Westin Hotel, Calgary, Alberta, on **Tuesday, May 19, 1998** at 2:30 p.m. Shareholders who are unable to attend are urged to complete, sign and mail their proxies to ensure their common shares will be voted at the meeting.

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□ CORPORATE HIGHLIGHTS

Financial highlights (\$millions except per share amounts and % change)			
	1997	1996	% change
Gross revenues	217.6	173.8	25
Cash flow	122.9	90.1	36
Basic per share	3.09	2.51	23
Fully diluted per share	3.01	2.43	24
Net income	37.2	23.8	56
Basic per share	0.94	0.66	42
Fully diluted per share	0.90	0.66	36
Capital expenditures, net	179.4	101.8	76
Long-term debt	169.5	134.9	26
Shareholders' equity	274.0	232.0	18
Total assets	584.8	464.7	26
Common Shares Outstanding (000s)			
Weighted average			
Basic	39,792	35,880	11
Fully diluted	43,323	39,201	11

Operations highlights			
	1997	1996	% change
Production (daily production)			
Oil and liquids (bbls/day)	12,604	11,483	10
Natural gas (mmcf/day)	164.8	129.0	28
Proven and probable reserves (year-end)			
Oil and liquids (mmbbls)	47.7	40.4	18
Natural gas (bcf)	638.4	515.0	24
Wells drilled			
Gross	162	121	34
Net	147	102	44
Undeveloped land (000s of acres)			
Gross	1,856	1,535	21
Net	1,563	1,318	19
Average working interest (%)	84	86	



Penn West's hands-on management team. From left: Dale Miller, manager, exploitation and operations; Donald J. Rae, vice president, exploration; Bryan Clake, manager, marketing; N. Murray Edwards, chairman; Gerry J. Elms, treasurer and secretary; William E. Andrew, president; Larry M. Jones, vice president, land and corporate development.

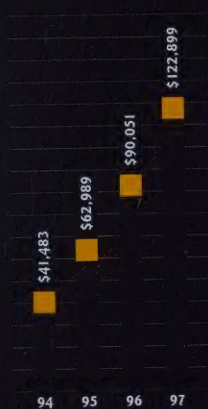


LETTER TO THE
SHAREHOLDERS

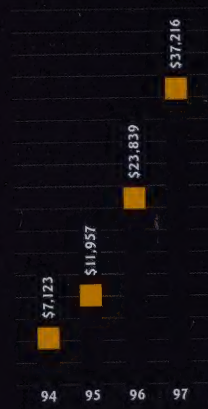
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Last year, we reported that Penn West had implemented a comprehensive strategy, had assembled an asset base and technical team and had launched a program of full-cycle exploration that, we predicted, was capable of generating continual, sustained growth in production, reserves, cash flow and net income. We are very pleased to report that Penn West, thanks to its solid base of producing and undeveloped assets and its focused, hands-on management team, succeeded in this task during 1997.

■



Cash Flow
(\$000s)



Net Income
(\$000s)



Drilling Activity

■ Gross Wells
■ Net Wells



Undeveloped Land
(000s of acres)

■ Gross
■ Net



Production

■ Natural Gas (mmcf/day)
■ Oil and Liquids (bbls/day)
(Totals in boe/day)



Reserves
Proven and Probable

■ Natural Gas (bcf)
■ Oil and Liquids (mmbbls)
(Totals in mmbbls)

Penn West achieved strong growth in production, reserves, cash flow and net income, meeting its key forecasts and setting new records in all these areas. The Company now has a five year track record of continual, year-over-year growth in the crucial operating and financial benchmarks that indicate sustained creation of shareholder value. Penn West has entered 1998 with a very strong balance sheet and is operationally poised to maintain further growth despite the current challenges in the oil price environment.

□ MAXIMIZING RESULTS...

Penn West's operating and financial results speak highly of our strategy, asset base and the competence and dedication of our head office and field operating teams.

Last year, Penn West increased daily average production to 29,100 boe per day, up from 24,400 boe per day in 1996, a gain of 19 percent. Our production in 1997 was levered towards natural gas with 165 million cubic feet per day of natural gas production and 12,600 barrels per day of crude oil and natural gas liquids production. Our 1997 exit rate was 30,500 boe per day, of which 57 percent was natural gas production.

In 1997, Penn West added 30.2 million boe of proven plus probable oil and natural gas reserves at a finding cost of \$5.93 per boe. Our reserve additions in 1997 were nearly three times 1997 production, giving us proven plus probable reserves at year-end of 638 billion cubic feet of natural gas and 47.7 million barrels of oil. Penn West's reserve-life-index now stands at 10 years, which represents a good balance between minimizing the risk of early depletion and maximizing current cash flow.

Penn West's year-over-year growth in oil and natural gas production has created a powerful financial engine. Five years ago, Penn West generated \$9.4 million in cash flow (\$0.56 per share). Last year, cash flow reached \$123 million (\$3.09 per share), an increase of 1,208 percent over four years and a gain of 36 percent over 1996.

Net income grew by 56 percent over the \$23.8 million (\$0.66 per share) achieved in 1996, reaching \$37.2 million (\$0.94 per share) in 1997.

Penn West has a very strong balance sheet. The Company's growth over the past two years has been financed primarily through cash flow, boosted by a moderate equity issue that has kept dilution to a minimum.

Since 1993, when the current management team took control of Penn West, we have focused on strengthening our balance sheet. Our debt- to-cash-flow ratio has been slashed from 2.66:1 in 1995 to 1.50:1 last year.

□ ...THROUGH HANDS-ON MANAGEMENT

Adding reserves means little if costs spiral out of control. An oil and natural gas producer's cash flow will quickly be consumed, and earnings per share will begin to slide, if the company cannot add reserves at reasonable finding and development costs. This was particularly true in last year's heated drilling environment, which drove up the cost of Crown lands and field services and saw many oil and natural gas producers run into cost control problems.

Penn West's management team has made it a priority to control all of the Company's costs: general and administrative, land acquisition, finding and development, and field operating. We are pleased to report that the Company's general and administrative costs declined by 9 percent last year, despite the addition of new staff, to \$0.30 net per boe of production.

Last year Penn West controlled its land costs by scaling back land acquisitions somewhat and sidestepping the rush of mergers and corporate acquisitions. Despite that, the Company was able to round out its base of undeveloped land and complete important acquisitions including a portfolio of producing properties and undeveloped land that make up the base of Penn West's new fifth Core Area in Southeast Saskatchewan.

Initially, Penn West grew through the low-cost acquisition of companies and property portfolios. As Penn West reached intermediate producer status and focused on the task of growing through the drillbit, we worked on operational efficiencies that help to control finding and development, and operating costs. These include operatorship of major natural gas processing plants, local dominance and medium-term, fixed-rate contracts for drilling rigs and other field services.

Consequently, Penn West has been able to maintain low finding and development, and operating costs. Our finding and development costs last year were \$5.93 per barrel, proven plus probable. While that is up from the \$5.33 per barrel achieved in 1996, the Company's four-year average finding and development cost remains a very favourable \$5.14 per barrel. In 1997, Penn West's operating costs averaged \$4.57 per barrel.

Penn West's management team is never "satisfied" with our cost performance. We will continue to work diligently to keep all of our costs as low as possible, thereby extracting the maximum possible financial benefits from our asset base.

□ FULL-CYCLE EXPLORATION WITH A NATURAL GAS FOCUS

Penn West's operations are guided by a comprehensive strategy developed by the Company's management team. The principal elements of this strategy are:

- Assemble and continue building a large base of undeveloped land that provides a balanced inventory of prospects for natural gas and oil exploration, development and exploitation;
- Focus activity in five Core Areas in the Western Canada Sedimentary Basin providing a diversity of prospects, mitigating exploration and commodities risks, offering the flexibility needed to adjust production volumes according to pricing opportunities and forming a strong foundation for long-term growth in production and reserves;
- Maintain a well-structured, focused program of full-cycle exploration that maximizes current production and cash flow, ensures near-term growth through development drilling and fuels longer-term growth through exploration;
- Attain a high working interest and operatorship in nearly all major projects, ensuring decision-making and cost control and maximizing returns to Penn West's shareholders; and
- Through hands-on management, rigorously control land acquisition, finding and development, operating, and general and administrative costs, thereby maintaining a high reinvestment ratio, providing for long-term growth in production and reserves and maximizing growth in shareholder value.

We will continue to work diligently to keep all of our costs as low as possible, thereby extracting the maximum possible financial benefits from our asset base.

Penn West's base of undeveloped land has increased from fewer than 200,000 net acres in 1993 to almost 1.6 million net acres in 1997, located almost exclusively within our Core Areas of activity. We have structured our land base to create a strong foundation for growth. It provides a mix of low-risk exploitation prospects that maximize current production and cash flow,

development prospects for near-term growth and exploration prospects that will add to natural gas and oil reserves and production over the longer term.

For the past several years, Penn West's operations had been focused among four Core Areas. These are the Northern, Peace River Arch, Central and Plains Areas. These areas provide a mix of already-producing properties and geologically promising undeveloped lands that offer a wide variety of internally generated exploration and development opportunities, plus a good mix of natural gas and oil prospects.

In each Core Area, we work to assemble a cohesive land base that provides high working interests plus dominance of adjacent lands to pursue future development prospects. In 1997, through an acquisition of a portfolio of properties made at favourable cost, Penn West added a fifth Core Area that provides more than 50,000 net acres of undeveloped land and allows Penn West to focus on light crude oil opportunities in Southeast Saskatchewan.

Penn West's large base of undeveloped land and diversified inventory of prospects provides Penn West with the critical mass needed to generate continuous, year-over-year gains in production through the drill-bit. During 1997 Penn West invested a total of \$179 million, drilling 147 net wells, conducting extensive geophysical work, adding to its land base and constructing or expanding several key facilities.

Penn West's large and varied inventory of prospects and its operational scale also provide the flexibility needed to re-balance production in order to take advantage of changes in commodities prices. Penn West produces only minimal volumes of heavy oil below 15 degrees API. The Company's average crude oil quality is 29 degrees API.

To take advantage of the strengthening in Alberta fieldgate natural gas prices that occurred through 1997, and believing prospects for further increases in natural gas prices remain strong, Penn West focused increasingly on natural gas production. By emphasizing exploration and development activities on natural gas rich properties, such as Wildboy in our Northern Area, Penn West will increase its natural gas weighting through 1998 to about 60 percent.

□ MOVING FORWARD

Despite the challenging oil price environment, Penn West expects to increase production and cash flow during 1998. Average daily production is forecast to increase to 33,400 boe/day, a gain of 15 percent year over year. Given the more positive price environment for natural gas, including the steady expansion of Western Canada's export pipeline capacity, we will continue to weight our production towards natural gas in the short term.

Our increase in production is forecast to include growth of 6 percent in crude oil and liquids production and 21 percent in natural gas production, to 200 mmcf per day. As in previous years, our exploration program is expected to more than replace reserves. Penn West plans to exit 1998 with total production of 36,000 boe per day.

By emphasizing exploration and development activities at several strong natural gas properties, particularly at Wildboy in our Northern Area, Penn West will increase its natural gas weighting through 1998 to about 60 percent.

One of the Company's foremost goals during 1998 is to protect the integrity of its balance sheet. While Penn West's strategy, focus and operating principles are holding up well in the current environment, it is important to exercise prudence with our budget. This year, our capital expenditures will total \$185 million. This budget will fund the drilling of 195 net wells in a program primarily concentrated on adding natural gas production and reserves.

With our planned growth in production volumes and further reductions in per barrel operating and administrative costs, we expect to increase cash flow in 1998 to \$125.6 million, or \$3.13 per share. Our net income for 1998 is forecast to be \$37.6 million or \$0.94 per share, unchanged from 1997.

We are basing our forecasts on an average W.T.I. price for the year of US\$17.65 per barrel. That is down almost \$3.00 per barrel from last year, and assumes a modest price recovery later in the year. We continue to forecast an increase in the average fieldgate price of natural gas, and expect to average \$2.00 per mcf at the wellhead in 1998.

We retain tremendous optimism about the medium- to longer-term prospects of the Western Canada Sedimentary Basin. Our measured response to the current pricing environment will keep Penn West financially strong and operationally poised to quickly resume more rapid growth as crude oil prices strengthen.

Maintaining our financial strength will also allow Penn West to respond to opportunities for acquisitions that add reserves and production at low cost or that represent either a strategic expansion or a genuinely good fit with Penn West's existing properties.

The most critical component of Penn West's future success is the sustained effort of our team, which includes more than 200 field, administrative and technical staff and management, without whose dedication the Company would not be on its current path. Our sincerest thanks go out to them, as well as to the members of Penn West's Board of Directors for their wisdom and counsel through the year.

On behalf of the Board of Directors,

A handwritten signature in black ink, appearing to be 'N. Murray Edwards'.

N. Murray Edwards
Chairman

A handwritten signature in black ink, appearing to be 'William E. Andrew'.

William E. Andrew
President

Improving efficiency at Minnehik-Buck Lake

Greg Gabert, operations



In 1996, the limited capacity of the natural gas processing plant that services Penn West's key Minnehik-Buck Lake natural gas and oil property placed an artificial ceiling on the Company's natural gas development potential in the area, and threatened to divert third-party processing business to a competing plant.

Recognizing the potential for natural gas development in the area, Penn West proceeded with a large-scale expansion aimed at improving environmental compliance, driving down unit processing costs and opening up potential for further natural gas development in the area. In a

\$12 million project completed in November 1996, the Minnehik-Buck Lake plant's inlet capacity was increased from 80 mmcf per day of natural gas to 128 mmcf per day.

"The increased capacity provides a substantial revenue netback, driving down processing costs and allowing us to begin tapping the area's full natural gas potential," says Greg Gabert.

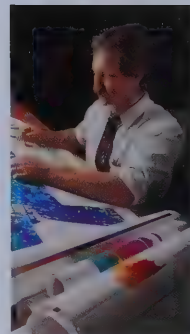


But the work didn't end at the plantgate—nor was it limited to natural gas. "Since the expansion, we've worked hard to reduce costs throughout the Minnehik-Buck Lake property," explains Gabert. "Where possible, we've consolidated our oil batteries into a single gathering system, reducing our maintenance, operating and repair costs." In 1998 Gabert's team will continue to focus on improving the plant's reliability and availability to maintain Penn West's record of maximizing profitability through continuous unit cost reductions.

During 1998 Penn West will provide additional third party processing capacity and is drilling a planned total of 15 natural gas wells with a view to further increasing production at the Minnehik-Buck Lake property.

Fabyan seismic and drilling program

Dan Koch, exploration



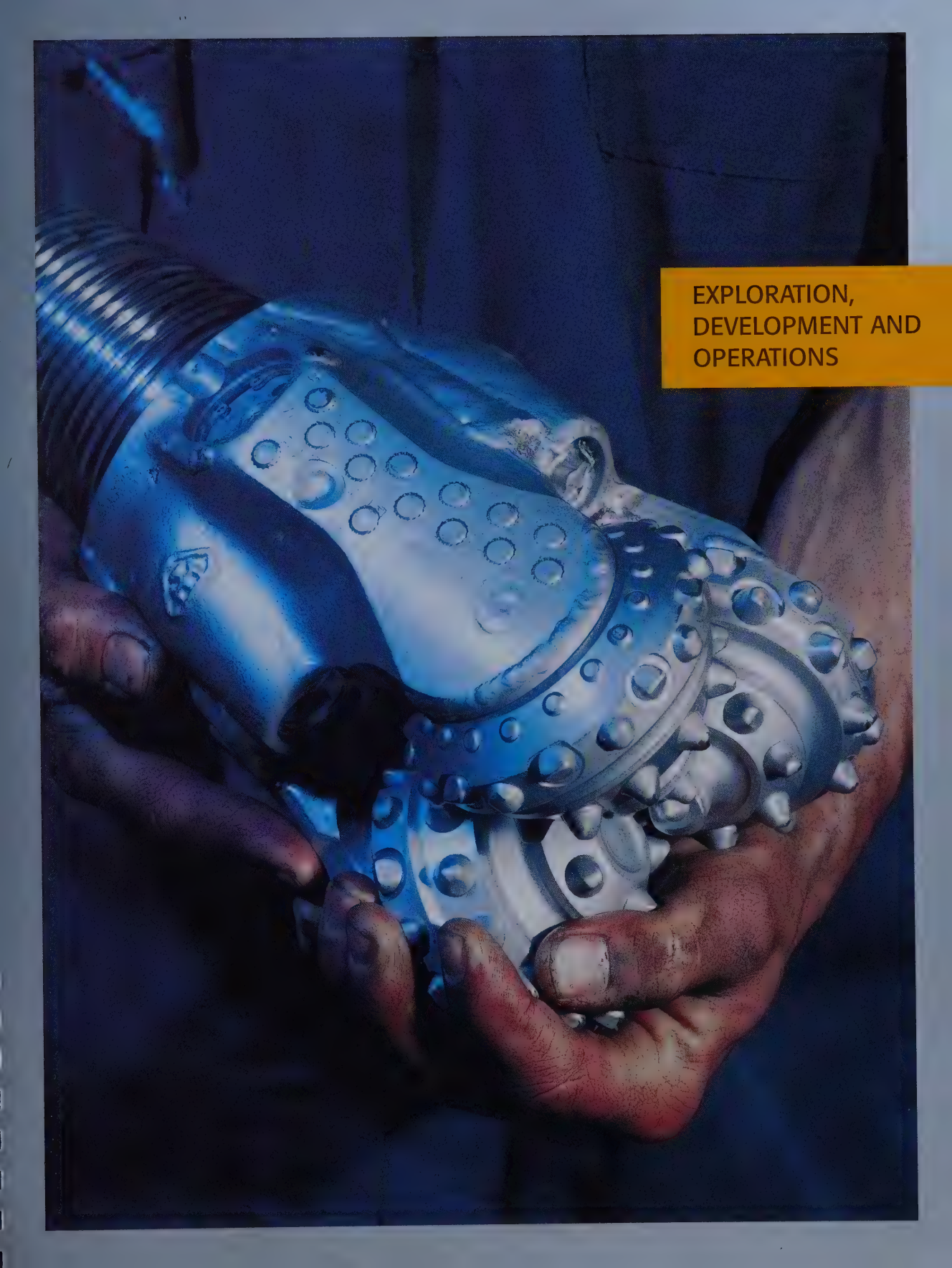
Another facility at which Penn West wanted to improve productivity in order to keep reducing the Company's overall unit costs was its Fabyan natural gas processing plant. During 1996, this Plains Area asset north of Wainwright, Alberta was operating at well below its processing capacity. The exploration team believed the area around Fabyan held natural gas potential in shallow Cretaceous-era formations. So in late 1996 an area exploration team led by Dan Koch launched an extensive seismic program in the area, shooting 55 km of 2-D seismic.

"With the restriction of being able to drill only one gas well per section, using 2-D is the most cost effective way to explore for shallow gas," says Koch. The new seismic data were combined with existing trade data, processed and interpreted as an integrated dataset. "Stratigraphic interpretation, coupled with amplitude versus offset techniques, revealed a number of anomalies which we believed were gas bearing zones," says the Penn West explorationist.



In 1997 Penn West began to exploit the area with an initial seven-well drilling program. "Every well successfully encountered gas pay with several wells having additional multi-zone potential for oil," says Koch of the program that added 8 million cubic feet per day of production.

Thanks to the success of our exploration team and the proximity of the Fabyan property to existing infrastructure, the Fabyan gas plant is now operating at capacity, helping to reduce Penn West's unit operating costs. This increased throughput has led to higher revenues for Penn West and reduced unit operating costs.



EXPLORATION,
DEVELOPMENT AND
OPERATIONS



Penn West's long-term program of full cycle exploration met with strong success through 1997. The Company achieved double-digit increases in production of natural gas and oil, discovered new reserves representing almost three times 1997 production levels, and through rigorous cost control transformed these technical achievements into strong financial results,



Our extensive base of undeveloped land and large inventory of prospects at various stages of development allowed Penn West to respond to signals in the commodity price environment and focus increasingly on natural gas during 1997. Our production is now weighted 57 percent towards natural gas, a ratio that will increase further during 1998.

However, the Company retains a strong belief in the long-term potential of oil. Penn West is scaling back planned increases in oil volumes during 1998, while conducting extensive exploration to ensure that oil production rates can be raised rapidly once prices recover.

□ DEVELOPMENT STRATEGY AND OPERATING PRINCIPLES

Penn West's strategy is to achieve long-term growth by sustaining continual, year-over-year, cost-effective increases in production and reserves primarily through the drillbit. The Company believes the Western Canada Sedimentary Basin holds enough high-quality, untapped natural gas and oil reserves to make such a strategy achievable if certain operating principles are implemented and strictly adhered to. During 1997 Penn West posted strong successes in all key operating measures.

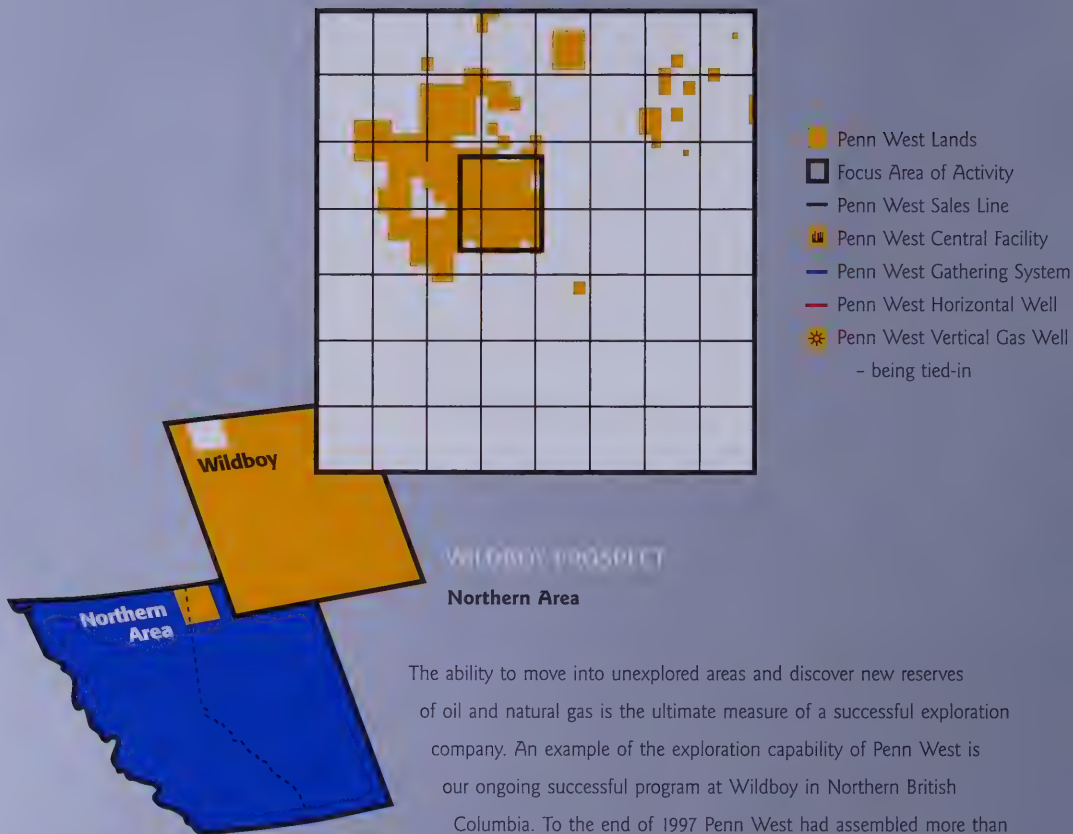
The following discussion describes Penn West's operating principles and explains how they have been implemented over the past several years.

Large Undeveloped Land Base

The foundation for long-term growth is undeveloped land. Through a combination of Crown purchases, property swaps and strategic acquisitions, Penn West has over the past five years assembled an undeveloped land base that at year-end 1997 had grown to 1.6 million net acres.

The Company's undeveloped land base is concentrated in five Core Areas of activity in western Canada. This undeveloped land base has been structured to provide a large inventory of natural gas and oil prospects of various types. At one end are low-risk, shallow-depth prospects adjacent to existing infrastructure that help the Company maximize current production and cash-flow. At the other end are deeper, higher-impact prospects in less explored areas that promise longer-term growth. In-between lie proven producing properties that contain extensive additional potential for development of multi-zone natural gas and oil-bearing formations.





The ability to move into unexplored areas and discover new reserves of oil and natural gas is the ultimate measure of a successful exploration company. An example of the exploration capability of Penn West is our ongoing successful program at Wildboy in Northern British Columbia. To the end of 1997 Penn West had assembled more than 100,000 acres of undeveloped land at Wildboy and had drilled 10 exploratory wells, which delineated 100 billion cubic feet of gas reserves in the Devonian Jean Marie formation. With three years of exploration and testing behind us we felt that 1998 was the year to begin to tap Wildboy's potential.



Natural gas horizontal drilling at Wildboy



To date in 1998 we have drilled and completed the six planned horizontal gas wells in the Jean Marie and we are on target to add 25 million cubic feet per day of new natural gas production in April.

The Wildboy gas project for winter 1997-1998 included installing 25 million cubic feet per day of compression capability and construction of a field gathering system to tie in six horizontal wells and five vertical wells. Natural gas will be shipped via a Penn West sales gas pipeline into Nova's Alberta system. We have planned for the future by over-designing our sales line to accommodate up to 75 million cubic feet per day of natural gas. In 1999, we plan to increase Wildboy's production to 40 million cubic feet per day.

□ CORE AREAS

CENTRAL

	undeveloped land (net acres)	production* oil and liquids (bbls/day)	natural gas (mmcf/day)
Minnehik-Buck Lake	54,000	2,000	26.0
Swan Hills	15,000	470	0.2
Otter	14,000	480	-
Heart River	20,000	-	6.0
Other	125,000	1,550	14.0
Sub-Total	228,000	4,500	46.2



PLAINS

	undeveloped land (net acres)	production* oil and liquids (bbls/day)	natural gas (mmcf/day)
Wainwright	128,000	2,210	19.0
Esther	168,000	1,500	5.2
Redwater	2,000	820	0.3
Hoosier	56,000	570	-
Other	117,000	890	9.9
Sub-Total	471,000	5,990	34.4

TOTAL ALL CORE AREAS

	undeveloped land (net acres)	production* oil and liquids (bbls/day)	natural gas (mmcf/day)
Total Core Areas	1,374,000	12,050	161.2
Non-Core Properties	189,000	1,050	12.8
Total All Properties	1,563,000	13,100	174.0

Average Working Interest 84%

* based on 1997 daily average exit volumes

PEACE RIVER ARCH

	undeveloped land (net acres)	oil and liquids (bbls/day)	production* natural gas (mmcf/day)
Progress	20,000	370	14.0
Saddle Hills	1,000	10	5.2
Buick Creek	19,000	50	5.2
Firebird	14,000	40	4.8
Pouce Coupe	22,000	40	2.2
Other	18,000	130	14.0
Sub-Total	94,000	640	45.4



NORTHERN

	undeveloped land (net acres)	oil and liquids (bbls/day)	production* natural gas (mmcf/day)
Boyer	300,000	130	30.0
Wildboy	105,000	-	-
Hotchkiss	10,000	-	3.0
Other	115,000	110	2.2
Sub-Total	530,000	240	35.2



SOUTHEAST SASKATCHEWAN

	undeveloped land (net acres)	oil and liquids (bbls/day)	production* natural gas (mmcf/day)
Flat Lake	51,000	680	-



BOYER PROSPECT

Northern Area

Penn West began to accumulate land, production and infrastructure at Boyer in northwest Alberta in 1993, with an eye to development of natural gas reserves and production in the shallow depth Bluesky, Gething and Banff zones. Beginning with initial production of 5 million cubic feet per day, Penn West has grown production to anticipated levels of 40 million cubic feet per day in early 1998, and has installed new processing facilities and gathering systems at Haig, Lennard Creek and Sousa.

In 1998, Penn West expects to drill 25 wells at Boyer. We plan to continue exploration and development in the area to exploit the significant low-cost gas potential into 1999 and beyond. Low risk development and exploration in areas like Boyer are primary building blocks for sustaining production and are premium opportunities for near-term growth at Penn West.



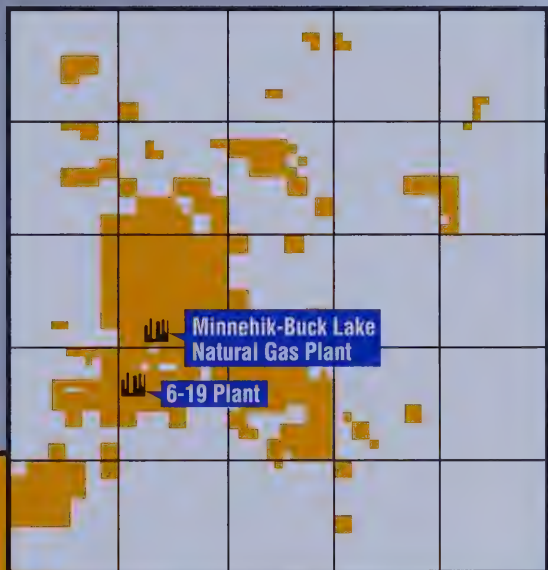
MINNEHIK-BUCK LAKE PROSPECT

Central Area

Penn West has assembled a formidable land position in the Pembina area of west-central Alberta. The area provides multi-zone potential for light oil and liquids-rich natural gas which Penn West will begin to exploit over the next several years and drilling prospects that range from shallow oil and natural gas in the Cretaceous to deep multi-million barrel opportunities in the Devonian.

Penn West's Minnehik property in Central Alberta is an important part of our plan for sustainable future growth. Exploration and development in the area had been focused since the 1960s on a large Mississippian Age Pekisko natural gas reservoir. Penn West sees numerous opportunities at Minnehik for untapped reserves both above and below the Pekisko. Our first task at Minnehik was to consolidate our land position and increase our working interest. With that accomplished we moved in late 1996 to modernize the Minnehik natural gas plant and increase inlet capacity to 128 million cubic feet per day.

In 1997 we acquired an extensive seismic database over our lands. Using this database we have identified numerous potential targets and we will be



drilling the first of a planned 15-well program during the second quarter of 1998. Production from these wells will have immediate impact as we have available capacity at Minnehik to handle additional volumes of liquids-rich natural gas.

Undeveloped land base (000s of acres)			
	1997	1996	1995
gross acres	1,666	1,535	1,571
net acres	1,564	1,318	1,206
average working interest (%)	84	86	77

At each of its chosen near-term development prospects, Penn West conducts substantial geophysical work, including lead shoots in prospective areas, close-in 2-D and 3-D seismic data acquisition on drilling prospects to reduce risk, and re-interpretation of existing seismic data stored in Penn West's extensive proprietary database.

Focus Activities on Core Areas

To improve cost control and mitigate exploration risk, Penn West focuses close to 100 percent of its exploration and development activities on its Core Areas.

The Company began 1997 with four Core Areas: the Northern, Peace River Arch, Central and Plains Areas.

During 1997 Penn West acquired a portfolio of properties in southeast Saskatchewan, which now form the Company's fifth Core Area. The Core Areas, which are discussed in detail on following pages, offer a full-range of natural gas and oil prospects, from near-term, low-risk to longer-term, higher-impact.

High Working Interests and Operatorship

Exercising direct operational control over field activities is a crucial element in allowing an oil and natural gas producer to control its destiny. High working interest maximizes the positive financial impact of natural gas and oil discoveries, while operatorship is crucial to controlling the nature and pace of development and maintain downward pressure on costs.

During 1997 Penn West attained an average working interest of 84 percent throughout its large inventory of prospects. The Company currently operates 75 percent of its natural gas and oil production.

Cost Control through Hands-on Management

The aforementioned principles all help Penn West attain a result that Company management considers absolutely crucial: cost control. If an oil and natural gas producer cannot maintain low finding and development, operating and general and administrative costs, profitable growth cannot be ensured.

By adhering to its proven strategy and by maintaining a hands-on team of management, technical, financial and operating staff who focus on cost control, Penn West has maintained low and in most cases declining unit costs in all key areas, thereby maximizing cash flow available for reinvestment and creation of long-term shareholder value. Penn West's field operations are now of a scale that allow the Company to lock in field and drilling services under fixed-rate, medium-term contracts, and to build and operate field processing facilities designed specifically for the Company's long-term needs.

Operational Agility

Due to the cyclical nature of commodity pricing, Penn West recognizes the importance of responding operationally to changes in oil and natural gas prices to maximize cash flow. The Company's sustained growth has given it a scale of operations and a diversity of prospects that allow Penn West to adjust its activities accordingly.

For the past several years, Penn West maintained an approximate balance of oil and natural gas production. Last year, the Company began to focus increasingly on natural gas, reaching a 57 percent natural gas weighting at year-end. However, this change in balance was achieved entirely through accelerated growth in natural gas output; no oil production was shut in. During 1998 Penn West will increase its natural gas weighting to a targeted 60 percent through double-digit increases in natural gas production and a smaller percentage growth in oil production. These principles served Penn West extremely well during 1997 and form the foundation for its continued growth through 1998 and beyond.

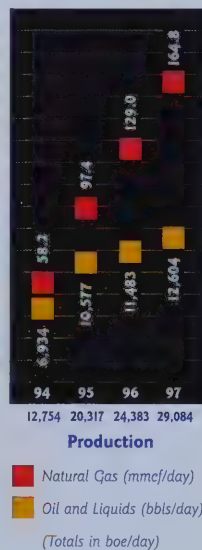
□ REVIEW OF CORE AREAS

Northern Area

The Northern Area is Penn West's main natural gas exploration asset. The region is one of the least-explored in the Western Canada Sedimentary Basin and contains massive potential for prolific, multi-zone natural gas finds. The Northern Area now represents 20 percent of the Company's natural gas production, a rapid increase from its grass-roots status only four years ago.

Penn West has assembled more than half a million acres of undeveloped land in its Northern Area. This land will provide not only years of development opportunities in existing producing areas, but will also provide opportunities for additional grass-roots prospects.

Penn West initially concentrated on production at its Boyer prospects, a group of natural gas properties which lie in the eastern reaches of the Northern Area



close to the Alberta-B.C. border. After discoveries at Haig, Lennard Creek and Sousa, Penn West brought natural gas production to 22 million cubic feet per day by early 1997.

Last year Penn West drilled 30 natural gas wells in the Boyer region, bringing production to 30 million cubic feet per day. The Company will continue to explore and develop its natural gas prospects during 1998.

Major producing fields in the Northern Area			
	undeveloped land (net acres)	oil and liquids (bbls/day)*	natural gas (mmcf/day)*
Boyer	300,000	130	30.0
Wildboy	105,000	-	-
Hotchkiss	10,000	-	3.0
Other	115,000	110	2.2
Total	530,000	240	35.2

*based on 1997 daily average exit volumes

Perhaps the most exciting play in Penn West's prospect inventory is the Wildboy natural gas play. Wildboy was the site of a Penn West discovery well into the Devonian Jean Marie in 1995, and to date Wildboy has met the great expectations which well testing and extensive 3-D seismic raised among our exploration team.

During 1997 Penn West began construction of facilities aimed at starting commercial production from Wildboy. During the first quarter of 1998 Penn West began a program of horizontal natural gas development wells, which will support production of 25 million cubic feet per day by April, 1998. Penn West believes the field will yield even more production and reserves over time and we plan to continue our aggressive development of the area in 1999.

The Northern Area contains numerous promising prospects for long-term growth in natural gas production and reserves. Exploration will continue at Wildboy and at Paddle Prairie, Lennard Creek and Haig during 1998 and beyond.

Peace River Arch Area

Penn West's Peace River Arch Area is a growing natural gas and light oil producing region. Penn West obtained its initial land position in the area in 1994 and cut its regional exploration teeth at the Progress prospect. Progress

Major producing fields in the Peace River Arch Area

	undeveloped land (net acres)	oil and liquids (bbls/day)*	natural gas (mmcf/day)*
Progress	20,000	370	14.0
Saddle Hills	1,000	10	5.2
Buick Creek	19,000	50	5.2
Firebird	14,000	40	4.8
Pouce Coupe	22,000	40	2.2
Other	18,000	130	14.0
Total	94,000	640	45.4

*based on 1997 daily average exit volumes

provided our exploration team with invaluable insight into the region's geological characteristics. Exploiting that expertise, Penn West began exploring aggressively for other natural gas finds in the region.

Over the past two years Penn West has followed up on its success at Progress with discoveries and development drilling at Saddle Hills, Buick Creek, Pouce Coupe and Firebird. Penn West drilled a total of eight natural gas wells on these prospects during 1997, bringing production at its Peace River Arch properties to 45 million cubic feet per day of natural gas and 640 barrels per day of oil and liquids. At year-end, the Peace River Arch Area was producing 5 percent of Penn West's oil and liquids and 26 percent of our natural gas.

The region contains excellent multi-zone potential ranging from shallow-depth Doe Creek zones to deeper Wabamun plays below 2,400 metres. During 1998 Penn West will continue to expand its natural gas production and conduct further exploration and development in this still under-explored region, focusing particularly on Buick Creek and Firebird.

Central Area

Penn West's Central Area is a proven natural gas- and oil-producing region that continues to present strong potential for growth in production and reserves through development and exploratory drilling. The Central Area generates 27 percent of Penn West's natural gas production and 34 percent of our oil and liquids production.

The principal property of our Central Area is Minnehik-Buck Lake. Over the past several years, Penn West has consolidated its land position,

Major producing fields in the Central Area			
	undeveloped land (net acres)	oil and liquids (bbls/day)*	natural gas (mmcf/day)*
Minnehik-Buck Lake	54,000	2,000	26.0
Swan Hills	15,000	470	0.2
Otter	14,000	480	-
Heart River	20,000	-	6.0
Other	125,000	1,550	14.0
Total	228,000	4,500	46.2

*based on 1997 daily average exit volumes

conducted geophysical work and launched a multi-year program to develop the region's untapped reserves.

During 1998 Penn West plans to drill 15 wells at Minnehik to tap medium-depth Belly River, Cardium, Viking, Glauconite, Ostracod, Nordegg and Mississippian horizons. With more than 200,000 acres of undeveloped land net to Penn West, the Central Area will furnish the Company with years of further development opportunities.

Plains Area

The Plains Area continues to provide the bulk of Penn West's oil production and, thanks to the Company's commanding land position of more than 470,000 net undeveloped acres, offers years of further low-risk, shallow-depth oil and natural gas exploration and development opportunities. The area, in east-central Alberta and southwestern Saskatchewan, contributed 46 percent of Penn West's oil production and 20 percent of our natural gas production at year-end 1997.

The Plains Area was the first region in which Penn West generated momentum in each phase of its full-cycle exploration program. Driven by our belief that millions of barrels of oil and billions of cubic feet of natural gas reserves lie untapped in this longstanding producing region, Penn West's goal was to explore and begin developing one major property and then, using the expertise gained, launch similar programs at several other prospects.

Starting in 1995, Penn West drilled discovery wells that identified million-barrel-plus oil finds at Esther and Hoosier. Penn West brought these medium- to heavy-gravity crude oil finds on production, then, after gaining a thorough understanding of the sub-surface through extensive use of 3-D seismic and

computerized reservoir modelling software, increased production and reserves through step-out drilling and enhanced recovery.

During 1996 and 1997 Penn West launched enhanced recovery programs at the Esther and Wildmere properties. A program of infill drilling was coupled with construction of oil batteries and water injection wells at each property to commence enhanced recovery by waterflooding. The waterfloods increased production levels significantly at both Wildmere and Esther.

Major producing fields in the Plains Area			
	undeveloped land (net acres)	oil and liquids (bbls/day)*	natural gas (mmcf/day)*
Wainwright	128,000	2,210	19.0
Esther	168,000	1,500	5.2
Redwater	2,000	820	0.3
Hoosier	56,000	570	-
Other	117,000	890	9.9
Total	471,000	5,990	34.4

*based on 1997 daily average exit volumes

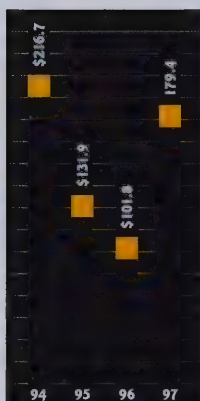
Even more important, the program doubled estimated ultimate oil recoveries, dramatically increasing Penn West's reserves and extending the productive life of each prospect. The current oil price environment will limit our development plans in the area in 1998, but we will continue to add prospects to our inventory to be exploited when oil prices recover.

The Plains Area also has natural gas potential. During 1997 Penn West continued drilling for shallow natural gas at its Wainwright prospect, bringing natural gas production there to 19 million cubic feet per day. During 1998 the Company plans to drill up to 80 natural gas prospects in the Plains Area. Our extensive existing infrastructure of processing plants and gathering lines will allow the natural gas to be developed at low cost.

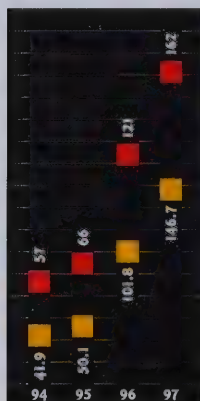
Southeast Saskatchewan Area

During 1997 an opportunity arose for Penn West to acquire a portfolio of producing properties and undeveloped land at favourable cost in Southeast Saskatchewan. This new region, which contains light-gravity crude oil in medium-depth Mississippian formations, was explored and drilled vertically during the 1960s and 1970s. Many producing fields offer strong potential for

revitalization through horizontal development drilling supported by modern, 3-D seismic interpretation, as well as potential for exploratory drilling into deeper formations.



Capital Expenditures
(\$ millions)



Drilling Activity

■ Gross Wells
■ Net Wells

Penn West's properties are currently producing a total of 680 barrels per day of crude oil. Penn West is expanding its land position and beginning to conduct some development drilling. During 1998 the Company will evaluate further opportunities for development and exploratory drilling as it continues to improve its understanding of this region's geological and operating characteristics.

□ 1997 CAPITAL PROGRAM

As in 1996, the focus of Penn West's capital program was sustaining growth through the drillbit, and Penn West was extremely active on all fronts of exploration and development. Our capital program for 1997 totalled \$179.4 million. Of this total, \$56 million was spent on drilling and completions, \$9 million was spent on geophysical data acquisition and analysis, \$16 million was spent on undeveloped land and \$38 million was spent on facilities.

Capital expenditures (\$ millions)			
	1997	1996	1995
Land	10.3	12.0	8.8
Net acquisitions	19.0	7.9	76.1
Drilling and completions	56.2	36.5	18.2
Facilities and well equipping	38.2	38.3	23.7
Geological and geophysical	9.8	6.8	4.8
Other	0.4	0.3	0.3
Capital expenditures	179.4	101.8	131.9

□ PRODUCTION, DRILLING AND RESERVES

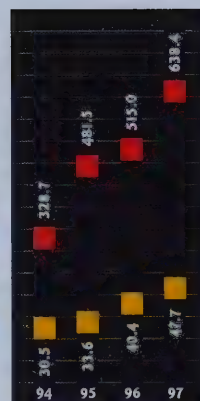
Penn West moved forward with an active and multi-faceted program of full-cycle natural gas and oil exploration at each of the four Core Areas with which we started the year. This program, the Company's largest to date, succeeded in increasing production and building our reserves. Penn West drilled a record total of 146.7 net wells in 1997, of which 12 were exploratory wells. Penn West achieved a success rate of 86 percent on a net basis for the year.

During 1997 Penn West increased its daily average production for the year by 19 percent to 29,084 boe, of which 12,604 barrels per day was oil and liquids production and 164.8 million cubic feet per day was natural gas production. Penn West exited 1997 with production of 30,500 boe per day, of which 57 percent was natural gas production.

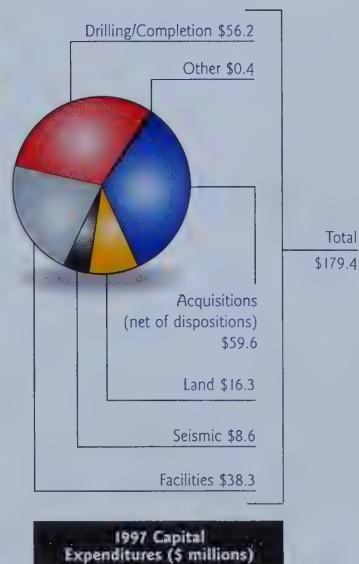
Penn West's exploration and development activities added new reserves totalling 30.2 million boe, or more than 280 percent of total production for the year. Reserves now stand at 47.7 million boe of crude oil and liquids and 638 bcf of natural gas. The reserve additions were achieved at an all-in finding and development cost of \$5.93 per barrel proven plus probable.

Drilling results						
	1997		1996		1995	
	gross	net	gross	net	gross	net
Oil	69	64.2	63	55.3	16	10.4
Natural gas	71	61.7	42	31.4	42	32.9
Dry	22	20.8	16	15.1	8	6.8
Total	162	146.7	121	101.8	66	50.1
Average working interest (%)	91		84		76	
Success rate (%)	86		87		88	

Finding and on-stream costs			
	1997	1996	1995
Net proven reserve additions (mmboe)	26.0	19.6	24.4
Average cost (\$/boe)	5.87	5.19	5.39
Net proven and probable reserve additions (mmboe)	30.2	19.1	25.8
Average cost (\$/boe)	5.93	5.33	5.11



Reserves Proven and Probable
 ■ Natural Gas (bcf)
 ■ Oil and Liquids (mmbbls)
 (Totals in mmboe)



Reserve values

	Reserves (before royalty)		Before tax discounted value of estimated future net revenues (\$ millions)			
	oil and liquids (mmbbls)	natural gas (bcf)	0%	10%	15%	20%
Proven producing	37.1	332.8	964.6	566.1	475.1	411.5
Proven non-producing	1.9	206.6	271.5	130.9	99.3	77.9
Total proven	39.0	539.4	1,236.1	697.0	574.4	489.4
Probable	8.7	99.0	292.2	94.9	64.5	46.6
December 31, 1997	47.7	638.4	1,528.3	791.9	638.9	536.0
December 31, 1996	33.6	481.5	1,165.5	587.0	465.6	384.8
December 31, 1995	30.5	328.7	918.2	445.7	351.2	289.2

Oil and liquids reserves (mmbbls, before royalties)

	1997	1996	1995
Proven producing	37.1	30.4	24.9
Proven non-producing	1.9	2.2	1.1
Total proven	39.0	32.6	26.0
Probable	8.7	7.8	7.6
Total	47.7	40.4	33.6
Reserve life index (years)*	10.0	9.4	7.9

*based on 1997 daily average exit volumes

Natural gas reserves (bcf, before royalties)

	1997	1996	1995
Proven producing	332.8	282.2	248.4
Proven non-producing	206.6	158.1	151.2
Total proven	539.4	440.3	399.6
Probable	99.0	74.7	81.9
Total	638.4	515.0	481.5
Reserve life index (years)*	10.1	10.3	11.7

*based on 1997 daily average exit volumes

Reserve additions (before royalty)

	oil and liquids (mmbbls)			natural gas (bcf)		
	proven	probable	total	proven	probable	total
December 31, 1994	22.7	7.8	30.5	262.7	66.0	328.7
discoveries and extensions	4.9	0.2	5.1	79.2	18.2	97.4
acquisitions/dispositions	4.5	0.1	4.6	103.5	9.6	113.1
production	(3.9)	-	(3.9)	(35.6)	-	(35.6)
revisions of prior estimates	(2.2)	(0.5)	(2.7)	(10.2)	(11.9)	(22.1)
December 31, 1995	26.0	7.6	33.6	399.6	81.9	481.5
discoveries and extensions	7.6	0.9	8.5	81.9	-	81.9
acquisitions/dispositions	3.2	(1.0)	2.2	11.2	(1.6)	9.6
production	(4.4)	-	(4.4)	(45.7)	-	(45.7)
revisions of prior estimates	0.2	0.3	0.5	(6.7)	(5.6)	(12.3)
December 31, 1996	32.6	7.8	40.4	440.3	74.7	515.0
discoveries and extensions	7.0	1.2	8.2	121.2	22.6	143.8
acquisitions/dispositions	4.9	-	4.9	39.8	3.8	43.6
production	(4.6)	-	(4.6)	(60.0)	-	(60.0)
revisions of prior estimates	(0.9)	(0.3)	(1.2)	(1.9)	(2.1)	(4.0)
December 31, 1997	39.0	8.7	47.7	539.4	99.0	638.4

Price forecast

	oil		natural gas
	WTI at Cushing, Oklahoma (\$US/bbl)	Light crude at Edmonton (\$Cdn/bbl)	TCGSL average field price (\$Cdn/mmbtu)
1998	20.52	27.23	1.79
1999	21.06	27.69	1.92
2000	21.61	28.43	2.02
2001	22.17	29.19	2.09
2002	22.75	29.97	2.18
2003	23.35	30.77	2.25
2004	23.96	31.59	2.32
2005	24.58	32.44	2.41

The estimate of future net production revenues at December 31, 1997, 1996, 1995 and 1994 was based on a price forecast used by Sproule Associates Limited in their independent report.

The forecast for oil prices is based on a benchmark price of West Texas intermediate crude oil delivered at Cushing, Oklahoma. This forecast was adjusted for transportation and quality differentials and translated to Canadian dollars at US\$1=Cdn\$.73 (US\$1.37=Cdn\$1) to reflect Edmonton Refinery postings for 40° API crude oil with a sulphur content of 0.4 percent.

Reserve quality and terms of applicable sales contracts are reflected in the natural gas price forecast. The TCGSL forecast is provided as a benchmark only.

□ NETBACKS

Penn West's hands-on approach to cost control is aimed at achieving the highest possible netbacks on natural gas and crude oil production. Despite the softening of oil prices, Penn West achieved strong netbacks during 1997.

Thanks to operating costs averaging \$4.57 per boe of production through the year, netbacks averaged \$11.84 per barrel of crude oil and liquids production, and \$1.32 per thousand cubic feet of natural gas production. The average oil netback was essentially unchanged from 1996, while the average natural gas netback showed a strong improvement of 15 percent over the previous year.

□ 1998 EXPLORATION AND DEVELOPMENT PROGRAM

Given the strength of Penn West's inventory of exploration and development prospects and our natural gas focus in the short term, the Company's management team intends to show continued growth in Penn West's productive capacity and reserves base during 1998.

Penn West has budgeted a total of \$185 million on exploration, development, seismic, land purchases and facilities for 1998. This budget will fund drilling of 195 net wells. Our drilling will be supported by extensive geophysical work at our key exploration and development prospects, including Wildboy, Minnehik, Wainwright, Esther-Hoosier and in the Peace River Arch. We are planning to increase natural gas production to 215 million cubic feet per day by year-end 1998, representing more than 60 percent of Penn West's total production on a barrel of oil equivalent basis.

Despite our natural gas focus, we are fully aware that the day will come when crude oil prices recover, and Penn West intends to be ready to exploit the opportunity. Penn West expects to increase oil and liquids production by about 6 percent during 1998, to 13,400 barrels per day. More importantly, we will continue to delineate additional reserves at several previous discoveries and drill a number of exploration wells at new prospects so we can rapidly increase oil production when the time is right.

Penn West's Northern Area will receive the bulk of natural gas exploration attention, with intensive horizontal natural gas drilling at Wildboy and further exploration and development at our Boyer prospects.

In the Peace River Arch area Penn West will continue building reserves and production of medium-depth light oil and shallow- to medium-depth natural gas.

Our Central Area contains numerous opportunities to increase natural gas, liquids and light oil production, and our Minnehik-Buck Lake and Pembina prospects will see the drilling of approximately 15 wells.

In our Plains Area we will work to build natural gas production while increasing our inventory of medium- to heavy-gravity crude oil prospects to position ourselves for rapid production increases in the future when oil prices recover.

Based on trends seen to date we believe that per acre bonuses for undeveloped land should soften during 1998. The strength of Penn West's balance sheet entering 1998 will allow the Company to use any weakness in commodity prices to continue building its base of undeveloped land at favourable prices. Sustained weakness in crude oil prices would also raise the likelihood of opportunities for low-cost acquisitions, and Penn West intends to remain open to transactions that could generate low-cost growth or further the diversification of our land base and prospect inventory.

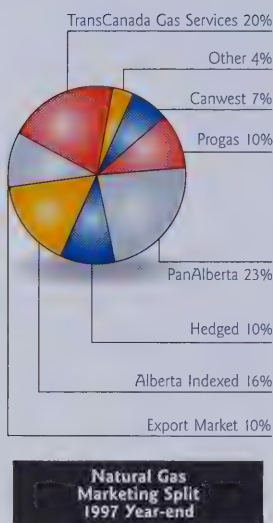
□ MARKETING

Penn West's marketing approach continues to reflect the following principles:

- Maximize production from existing assets and avoid any shut-in production due to marketing constraints;
- Diversify natural gas pricing on a geographic basis in order to maintain competitive prices; and
- Selectively hedge a portion of revenues to secure capital programs and allow for more efficient reinvestment.

Natural Gas Marketing

Penn West was able to produce its natural gas reserves at rates of take approaching 100 percent through the efficient use of firm transportation and through the active management of field nominations. This was achieved along with an average price of \$1.96/mcf in 1997 and a strong fourth quarter price of \$2.27/mcf. Penn West remains optimistic about the pricing outlook for natural gas following start-up of the Northern Border and TCPL pipeline expansions. These expansions, which are scheduled to commence in November of 1998, are expected to de-bottleneck Alberta markets and allow Alberta prices to track more closely with U.S. prices. This is in contrast to recent years when Alberta prices have traded at a significant discount to U.S. prices.



The chart to the left outlines Penn West's sales portfolio at the end of 1997. Gas sales were split approximately 60 percent to aggregators and 40 percent to direct sales.

Moving forward into 1998, Penn West expects to increase its exposure to Alberta index markets over the course of the year in order to position for the expected improvement in Alberta pricing fundamentals.

Oil and Liquids Marketing

Once again in 1997, Penn West was able to maintain 100 percent takes from the Company's oil properties. During 1997, the company hedged oil volumes of 2,500 barrels per day (representing 25 percent of 1997 oil production) at WTI prices averaging \$CDN 27.29/barrel. Going into 1998, the company has hedged 2,000 barrels per day of oil at WTI prices averaging \$CDN 27.68/barrel. Penn West will continue with its on-going program to maximize netbacks from all crude oil production in 1998.

ENVIRONMENTAL MATTERS

The oil and natural gas industry is subject to environmental regulations pursuant to a variety of provincial and federal legislation. Such legislation provides for restrictions and prohibitions on releases or emission of various substances produced in association with oil and gas operations. In addition, such legislation requires that well and facility sites be abandoned and reclaimed to the satisfaction of provincial criteria. Compliance with such legislation can require significant expenditures and a breach of such requirements may result in the imposition of material fines and facility closures.

The petroleum industry has initiated programs to minimize the environmental impact from oil and natural gas exploration and development, and Penn West is fully committed to meeting its responsibilities in this important area. The Company also recognizes the interests of other land users in resource development areas, conducting its operations accordingly. Penn West's Environmental Policy and Environmental Management Plan (EMP) encompasses the full range of air, water, soil and waste issues associated with oil and natural gas development. The EMP includes guidelines to 11 key areas that must be considered in conjunction with oil and natural gas development plans. These guidelines help ensure safe and environmentally sound field operations. Penn West's employees are trained in the objectives and implementation of the EMP.

Penn West conducts a program of detailed inspections, audits and environmental testing to assess the environmental liabilities that will be incurred during the eventual decommissioning and reclamation of its field facilities. Penn West pursues a program of environmental impact reduction aimed at reducing these future corporate liabilities without hampering field productivity. This program, launched in 1994 and ongoing into 1998, includes measures such as removing flare pits, reclaiming spill sites and abandoning unproductive wells.

Penn West's environmental programs are monitored to ensure that they comply with all government environmental regulations and with the Company's own environmental policies. The results of these programs are reviewed with Penn West management and operations personnel through regular stewardship reports.

□ DIRECTORS AND OFFICERS

A complete listing of the Directors of the Company and related information can be found in the Information Circular and Proxy Statement dated April 14, 1998 under the heading "Election of Directors", which information is incorporated herein by reference. The other officers of the Company are Larry M. Jones, Vice President Land and Corporate Development, Donald J. Rae, Vice President Exploration and Gerry J. Elms, Treasurer and Secretary. Mr. Jones has been Vice President Land and Corporate Development of the Company since May 1995, prior thereto was Land Manager of the Company since December 1992. Mr. Rae has been Vice President Exploration of the Company since January 1997 and prior thereto was Exploration Manager of the Company since April 1993. Mr. Elms has been the Treasurer of the Company since March 1998 and prior thereto was the Controller of the Company since June 1994.

Wildmere waterflood

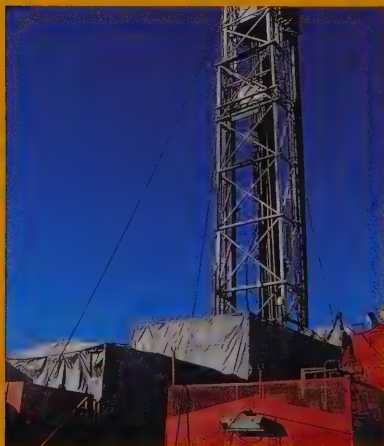
Ken Pyo, engineering



Penn West's waterflood at its Wildmere heavy oil property is an example of how a longstanding producing field can be given a new lease on life through cost-effective application of enhanced recovery techniques. Previously, operators had sought to boost production by injecting water at the south and north ends of this Sparky sandstone field.

"Sparky sands are very suitable for waterflood. They've proven themselves very responsive to that technique," explains Ken Pyo. "But the previous method of waterflood did not permit proper sweep of the oil in the main part of the reservoir."

Last year, Penn West's exploitation group proposed an optimization program to implement a better waterflood method at the property, which was acquired in 1996. Pyo says that, because the reservoir had good well control and its geology was well-understood, conventional reservoir engineering



methods and pressure data from producing wells were sufficient to plan the waterflood. Starting late last year, Penn West drilled new infill wells and converted three additional injection wells. In 1998, three more strategically located producing wells will be converted to injection.

"The initial reservoir response is very good," says Pyo. "We're starting to see fluid levels going up at the adjacent producing wells already." Penn West believes the waterflood will boost ultimate oil recovery at Wildmere, increasing the property's proven developed reserves by 1 million barrels and extending the field's economic life by at least eight years.

Wildboy natural gas transportation and marketing

Nancy Ames, marketing



As Penn West's exploration team geared up to develop its natural gas discovery at Wildboy, the marketing team went to work to ensure there was adequate pipeline capacity and strong markets for the field when it came on-stream in March 1998. After comparing service options and market reach, Penn West decided to connect the Wildboy field to Nova Gas Transmission's line at Shekile River North in northern Alberta. "This provides access not only to Alberta markets, but to export markets in the U.S. Midwest, Northeast and Eastern Canada," explains Nancy Ames.

All six horizontal gas wells at Wildboy have been completed, and results to date are meeting expectations. For next year, says Ames, Penn West will evaluate several alternatives for handling increased production volumes out of Wildboy.

Wildboy's initial production of 25 million cubic feet per day is now being sold into strengthening Alberta markets in Penn West's Alberta Direct Pool. "We act as our own aggregator," says Ames. "We bring gas from 55 receipt



points together into our Nova account, and allocate it from there." Penn West markets gas under a variety of daily to one-year contracts to Alberta customers. "Doing it this way allows us to save marketing fees, and lets us structure our sales portfolio to take advantage of prices," says Ames. "With the expansion of export pipeline capacity providing the prospects for stronger gas prices within Alberta, we're looking to have more exposure to Alberta markets."

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MANAGEMENT DISCUSSION AND ANALYSIS



Penn West was successful again in 1997 in meeting or

exceeding its targets for growth in production volumes,

revenues, cash flow and net income, while maintaining low finding,

operating and corporate costs. Growth was achieved primarily

through the drillbit, combined with a strategic acquisition of

a portfolio of properties which consolidated Penn West's position

in its existing Core Areas and provides potential for growth

in a new Core Area in Southeast Saskatchewan.



In 1997 Penn West continued to implement the key operating principles underlying its long-term strategy of sustaining growth and maximizing profitability through a well-managed, cost-effective program of full-cycle exploration. These key principles are:

- Consolidating its position in core areas through land and property acquisitions;
- Exploiting its asset base through effective use of infrastructure and executing low risk development projects;
- Conducting new exploration plays to ensure future growth; and
- Focusing on economic projects and containing costs as industry activity levels continue to increase.

This strategy will be effective during the inevitable upswings or downturns in the commodity price environment. The Company's operational agility allowed it to shift towards a more natural gas-weighted production balance through 1997 as the price environment changed.

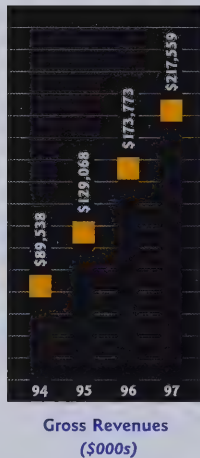
□ OIL AND NATURAL GAS REVENUES

Oil and natural gas revenues (\$000s)		Years ended December 31	
	1997	1996	1995
Oil and liquids	\$ 99,862	\$ 91,614	\$ 76,667
Natural gas	117,697	82,159	52,401
	\$ 217,559	\$ 173,773	\$ 129,068

Revenues from oil and liquids increased by 9 percent to \$99.9 million in 1997 from \$91.6 million in 1996. This increase is attributable to the 10 percent increase in the Company's average daily production to 12,604 bbls/day in 1997 from 11,483 bbls/day in 1996. This increase was somewhat offset by a drop in average prices received for oil and liquids to \$21.71/bbl in 1997 from \$21.80/bbl in 1996.

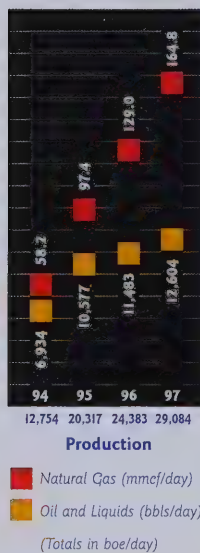
Revenues from natural gas increased by 43 percent in 1997 to \$117.7 million from \$82.2 million in 1996. The increase in natural gas revenues resulted from a 28 percent increase in average natural gas production to 164.8 mmcf/day in 1997 from 129.0 mmcf/day in 1996 and a 13 percent increase in the average natural gas price received by Penn West to \$1.96/mcf in 1997 from \$1.74/mcf in 1996.

The improved financial results for both main commodities were driven primarily by the Company's ongoing success in sustaining a cost-effective program of full-cycle exploration at each of its five Core Areas.



1997 increases in gross revenues (\$000s)	
Gross revenues - 1996	\$ 173,773
Increase in oil and liquids production	8,673
Decrease in oil and liquids price	(445)
Increase in natural gas production	22,467
Increase in natural gas price	13,091
Gross revenues - 1997	\$217,559

□ ROYALTY EXPENSES



Royalty expenses	Years ended December 31		
	1997	1996	1995
Royalties, net of Alberta			
Royalty Credit (\$000s)	\$ 34,875	\$ 29,401	\$ 17,044
Average cost (\$/boe)	\$ 3.29	\$ 3.29	\$ 2.30
Percentage of gross revenues	16%	17%	13%

The average royalty rate Penn West incurred in 1997, net of the Alberta Royalty Credit, was 16 percent, a decrease of 1 percent from 1996. The average royalty per boe of production remained unchanged at \$3.29. The rate decrease reflects a lower oil and liquids royalty rate of 18 percent, down from 20 percent in 1996, due to the reduced impact of hedging losses in 1997. The average natural gas royalty rate increased slightly to 15 percent in 1997 from 14 percent in 1996, due to higher Crown royalty rates associated with the higher natural gas prices received in 1997 versus 1996.

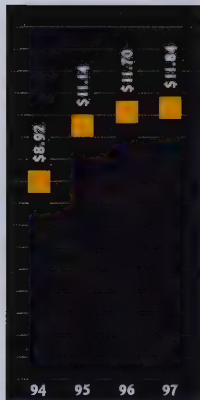
□ OPERATING EXPENSES

Operating expenses	Years ended December 31		
	1997	1996	1995
Operating expenses (\$000s)	\$ 48,555	\$ 40,975	\$ 33,287
Average cost (\$/boe)	\$ 4.57	\$ 4.59	\$ 4.49
Percentage increase (decrease) over previous year	8%	2%	(15%)
Percentage of gross revenues	22%	24%	26%

Penn West operates 75 percent of its total production, providing optimal control over operating methods and costs. In 1997, field operating costs averaged \$4.57/boe, a slight decrease from the average cost of \$4.59/boe achieved in 1996.

Operating costs for oil and liquids increased by 4 percent to \$6.00/bbl in 1997 from \$5.76/bbl in 1996 due to an escalation of field service costs driven by the higher industry-wide levels of exploration and development activity. Operating costs for natural gas in 1997 were \$0.35/mcf (\$3.50/boe), unchanged from 1996. Penn West's overall operating costs decreased due to the Company's increased weighting of natural gas production in 1997.

□ NETBACKS



Netbacks: Oil and Liquids (\$/bbl)

Netbacks	Years ended December 31		
	1997	1996	1995
Oil and liquids			
Production (bbls/d)	11,604	11,483	10,577
Price (\$/bbl)	\$ 21.71	\$ 21.80	\$ 19.86
Royalties, net (\$/bbl)	(3.02)	(4.34)	(3.19)
Operating expenses (\$/bbl)	(6.00)	(5.76)	(5.53)
Netback (\$/bbl)	\$ 11.84	\$ 11.70	\$ 11.14
Natural gas			
Production (mmcf/d)	154.8	129.0	97.4
Price (\$/mcf)	\$ 1.96	\$ 1.74	\$ 1.47
Royalties (\$/mcf)	(0.19)	(0.24)	(0.13)
Operating expenses (\$/mcf)	(0.35)	(0.35)	(0.33)
Netback (\$/mcf)	\$ 1.32	\$ 1.15	\$ 1.01



Netbacks: Natural Gas (\$/mcf)

The Company's lower royalty rates on oil and liquids production more than offset the decline in average prices received and the slight increase in operating costs incurred. In 1997, Penn West received an average oil and liquids netback of \$11.84/bbl, an increase of 1 percent from \$11.70/bbl netted back in 1996. An increase in natural gas prices of 13 percent in 1997 over 1996, resulted in natural gas netbacks increasing by 15 percent to \$1.32/mcf in 1997 from \$1.15/mcf in 1996.

□ GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses		Years ended December 31		
	1997	1996	1995	
Gross expenses (\$000s)	\$ 10,980	\$ 9,491	\$ 8,691	
Operator recoveries (\$000s)	(5,412)	(4,678)	(3,344)	
Capitalized expenses (\$000s)	(2,380)	(1,846)	(1,420)	
	\$ 3,188	\$ 2,967	\$ 3,927	
Gross general and administrative expenses - average cost (\$/boe)	\$ 1.03	\$ 1.06	\$ 1.17	
Percentage of gross revenues	5%	5%	7%	
Net general and administrative expenses - average cost (\$/boe)	\$ 0.30	\$ 0.33	\$ 0.53	
Percentage of gross revenues	1%	2%	3%	

Gross general and administrative expenses increased due to the increase in staff levels resulting from the Company's expanding asset base and production levels. However, when expressed on a per barrel of oil equivalent basis, the gross general and administrative costs decreased by 3 percent, to \$1.03/boe in 1997 from \$1.06/boe in 1996.

This level of costs reflects Penn West's continual increases in corporate productivity that have been in evidence over the last three years. Net general and administrative expenses decreased by 9 percent to \$0.30/boe in 1997 from \$0.33/boe in 1996, reflecting the growth in the number and proportion of assets operated by the Company, and related recoveries.



General and Administrative Expenses

■ Gross (\$/boe)
■ Net (\$/boe)

□ FINANCING EXPENSES

Financing expenses (\$000s)		Years ended December 31	
	1997	1996	1995
Interest	\$ 6,745	\$ 9,488	\$ 10,929
Cash flow times interest coverage	14.1	10.5	6.8
Average cost (\$/boe)	\$ 0.04	\$ 1.06	\$ 1.48
Percentage of gross revenues	2%	5%	8%

Interest expense for the year ended December 31, 1997 amounted to \$6.7 million, a decrease of 29 percent from \$9.5 million in 1996. This decrease resulted from lower average debt levels in 1997 as a result of the equity financing completed in October 1996 and from lower interest rates experienced in 1997.

□ DEPLETION AND DEPRECIATION

Depletion and depreciation (\$000s)		Years ended December 31	
	1997	1996	1995
Depletion and depreciation	\$ 45,379	\$ 39,376	\$ 36,824
Current site restoration provision	7,250	3,392	1,604
	\$ 52,629	\$ 42,768	\$ 38,428
Average cost (\$/boe)	\$ 4.96	\$ 4.79	\$ 5.18
Percentage of gross revenues	24%	25%	30%

Depletion, depreciation and the site restoration provision increased by 23 percent to a total of \$52.6 million in 1997 from \$42.8 million in 1996. This was a direct result of increases in the Company's production levels combined with an increase in the rate used for providing for future site restoration and abandonment costs. Average unit costs increased by 4 percent to \$4.96/boe in 1997 from \$4.79/boe in 1996. The limited increase in the depletion and depreciation rate reflects Penn West's continued low finding and on-stream costs.

□ TAXES

Taxes (\$000s)	Years ended December 31		
	1997	1996	1995
Deferred income taxes	\$ 33,054	\$ 23,371	\$ 12,677
Capital taxes	\$ 1,297	\$ 964	819
	\$ 34,351	\$ 24,335	\$ 13,496
Effective tax rate	48.0%	50.5%	53.0%

The provision for deferred income taxes rose by 41 percent to \$33.1 million in 1997 from \$23.4 million in 1996. This is because of continuing growth in net income before taxes, which increased by 49 percent year over year. The Company's effective tax rate declined slightly to 48 percent in 1997 from 50.5 percent in 1996.

Capital taxes increased by 35 percent in 1997 to \$1.3 million from \$1.0 million in 1996 due to the increase in shareholders' equity resulting from the equity issue completed in October 1996.

□ CASH FLOW AND NET INCOME

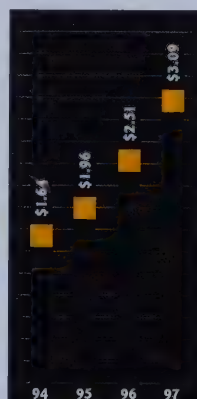
Cash flow and net income rose significantly in 1997 over 1996, meeting Company forecasts, due to significant increases in production, higher natural gas prices and lower interest costs. On a unit of production basis, operating costs declined slightly, while depletion and depreciation increased by 4 percent. Viewing these costs on a percentage of revenue basis, both operating costs and depletion and depreciation showed year over year improvements of 2 percent and 1 percent, respectively.

Cash flow increased by 36 percent to \$122.9 million in 1997 from \$90.1 million in 1996. Basic cash flow per share increased by 23 percent, reaching \$3.09 in 1997, compared to \$2.51 in 1996.

Net income grew by 56 percent to \$37.2 million in 1997 from \$23.8 million in 1996. Basic net income per share increased by 42 percent in 1997 to \$0.94 from \$0.66 in 1996.



Cash Flow
(\$000s)



Cash Flow Per Share
(\$ basic)

Items affecting cash flow and net income				Years ended December 31			
	1997			1996		1995	
	\$/boe	%		\$/boe	%	\$/boe	%
Oil and natural gas	\$20.50	100.0		\$19.47	100.0	\$17.41	100.0
Net royalties	(3.29)	(16.1)		(3.29)	(16.9)	(2.30)	(13.0)
Operating expenses	(4.57)	(22.3)		(4.59)	(23.6)	(4.49)	(26.0)
Net operating income	12.64	61.6		11.59	59.5	10.62	61.0
General and administrative	(0.30)	(1.5)		(0.33)	(1.7)	(0.53)	(3.1)
Interest	(0.64)	(3.0)		(1.06)	(5.4)	(1.48)	(8.5)
Capital taxes	(0.12)	(0.6)		(0.11)	(0.6)	(0.11)	(0.6)
Cash flow from operations	11.58	56.5		10.09	51.8	8.50	48.8
Depletion and depreciation	(4.96)	(24.2)		(4.79)	(24.6)	(5.18)	(29.8)
Deferred taxes	(3.11)	(15.2)		(2.62)	(13.5)	(1.71)	(9.8)
Net income	3.51	17.1		\$2.68	13.7	\$ 1.61	9.2

□ LIQUIDITY AND CAPITAL RESOURCES

Capitalization						
	1997		1996		1995	
	\$000s	%	\$000s	%	\$000s	%
Common share equity, at market	\$618,064	77.0	\$549,962	80.7	\$239,375	58.8
Long-term liabilities	169,468	21.1	134,880	19.8	159,388	39.2
Working capital deficiency (surplus)	14,746	1.9	(3,248)	(0.5)	8,170	2.0
	\$602,278	100.0	\$681,594	100.0	\$406,933	100.0

Financial markets continued to recognize Penn West's performance and further potential throughout 1997. Market capitalization increased by 12 percent, while cash flow per share increased by 23 percent.

Penn West's closing market price on The Toronto Stock Exchange was \$15.45 per share in 1997, \$14.00 per share in 1996 and \$6-7/8 per share in 1995. Market capitalization rose from \$239 million at year-end 1995, to \$550 million in 1996 and to \$618 million in 1997.

Penn West remains solidly financed. The Company's debt-to-cash flow ratio at year-end 1997 stood at 1.5:1, a significant decrease from the ratio of 2.66:1 in 1995. This two-year improvement was driven by the Company's strong growth in production and cash flow and by an issue of equity capital completed in late 1996.

Penn West's strong financial position will allow the production increases planned for 1998 and other programs requiring capital investment to be completed while maintaining a total debt-to-cash flow ratio of less than 2:1.

Penn West has an aggregate borrowing limit of \$270 million on its loan facility with a syndicate of Canadian chartered banks, on which the Company had drawn approximately \$169.5 million at year-end 1997, leaving approximately \$100.5 million available. This loan facility is subject to an annual review by the lenders and requires no principal repayments provided that certain covenants with respect to asset coverage tests are met. These asset coverage tests are within Penn West's reserve base.

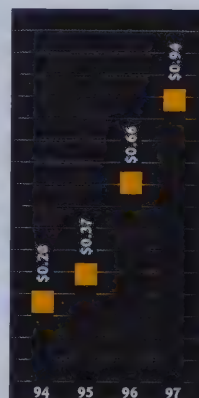
Penn West will fund its 1998 planned capital spending program of \$185 million from its cash flow, estimated at \$125.6 million, and from the aforementioned loan facility. The Company has sufficient capital to replace estimated 1998 production and to continue generating longer term growth.

□ BUSINESS RISKS AND PROSPECTS

The Company's exploration, development, production and acquisition activities are conducted in the Western Canada Sedimentary Basin and involve a number of business risks. These risks include the uncertainty of replacing annual production and finding new reserves on an economic basis, and the instability of commodity prices, foreign exchange rates and interest rates. To the extent practical, these risks are mitigated by the Company by employing highly trained and competent management and staff who manage these risks as follows:



**Net Income
(\$000s)**



**Net Income Per Share
(\$ Basic)**

- Balance production portfolio between oil and natural gas;
- Pursue numerous investment opportunities, including:
 - Low risk development projects;
 - Moderate risk exploration plays;
 - Strategic acquisitions; and
- Maintain low finding, operating and general and administrative costs

The Company's management team believes that these principles, validated through Penn West's five-year track record of growth and profitability, position the Company strongly to continue on a track of sustained growth in production volumes and creation of shareholder value.

The oil and natural gas industry is subject to extensive government influence through taxation policies and environmental legislation. Taxation policy has remained stable within a reasonable operating environment, however there is always the potential for change.

The industry is also subject to extensive regulations imposed by governments related to the protection of the environment. Environmental legislation in western Canada has undergone major revisions that have resulted in environmental standards and compliance becoming more stringent. The Company is committed to meeting its responsibilities to protect the environment wherever it operates and has instituted a series of controls and procedures with respect to environmental protection that meet the standards of the Environmental Code of Practice published by the Canadian Association of Petroleum Producers.

Most businesses rely heavily on computer information systems and computer hardware in their day-to-day operating activities. Under the Toronto Stock Exchange By-law No. 685, Listed Issuers are required to report on, including disclosure of material information concerning, the information systems issues and related business implications and uncertainties resulting from the Year 2000 century change. Management and the Board of Directors have reviewed the vulnerability of the Company to the Year 2000 issue, particularly as it relates to control systems for production facilities and business information systems. Plans have been developed and work is in progress to ensure significant issues are identified and resolved prior to the next fiscal year end.

The costs incurred to date and anticipated to be incurred in the future are not considered to be significant.

Despite dramatically lower oil and liquids prices, Penn West's growth pattern that commenced in 1993 is expected to continue in 1998, with forecasted cash flow of \$125.6 million or \$3.13 per share, an increase of 2 percent and 1.5 percent, respectively over 1997. This planned increase in cash flow is forecast to be achieved through increased production levels, with natural gas prices in 1998 forecast to be similar to 1997 levels and oil and liquids prices anticipated to be 11 percent lower than those achieved in 1997. The Company continues to hedge crude oil production, with 2,000 bbls/day having been sold forward in 1998. In addition, an average of 12 mmcf/d of natural gas has been sold forward in 1998. Penn West's development projects in 1998 will be weighted towards natural gas based on the favorable commodity price outlook.

The results of operations and the forecast noted above are sensitive to changes in production, commodity prices, foreign exchange rates and interest rates. The following table summarizes those sensitivities:

Sensitivities		
	impact on 1998 cash flow	impact on 1998 net income
Change of:		
Cdn \$1.00/bbl in oil price (\$000s)	\$ 4,000	\$ 2,200
Per Common Share	\$ 0.10	\$ 0.05
500 bbls/day in daily oil production (\$000s)	\$ 2,600	\$ 1,430
Per Common Share	\$ 0.06	\$ 0.04
\$0.10/mcf in natural gas price (\$000s)	\$ 5,100	\$ 2,800
Per Common Share	\$ 0.13	\$ 0.07
5,000 mcf/day in daily natural gas production (\$000s)	\$ 2,800	\$ 1,540
Per Common Share	\$ 0.07	\$ 0.04
\$0.01 in US\$/Cdn\$ exchange rate (\$000s)	\$ 1,600	\$ 880
Per Common Share	\$ 0.04	\$ 0.02
1% in prime interest rate (\$000s)	\$ 2,400	\$ 1,320
Per Common Share	\$ 0.06	\$ 0.03

□ MANAGEMENT'S REPORT

The consolidated financial statements of Penn West Petroleum Ltd. were prepared by management in accordance with accounting principles generally accepted in Canada. The financial and operating information presented in this report is consistent with that shown in the financial statements.

Management maintains a system of internal controls to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of relevant, reliable and timely financial information.

External auditors appointed by the shareholders have examined the consolidated financial statements. The Audit Committee, consisting of a majority of non-management directors, has reviewed these consolidated financial statements with management and the auditors and has reported to the Board of Directors. The Board has approved the consolidated financial statements.



Gerry J. Elms
Treasurer and Secretary
March 13, 1998



William E. Andrew
President

□ AUDITORS' REPORT

To the Shareholders of Penn West Petroleum Ltd.:

We have audited the consolidated balance sheets of Penn West Petroleum Ltd. as at December 31, 1997 and 1996 and the consolidated statements of income and retained earnings and changes in financial position for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1997 and 1996 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Calgary, Alberta,
March 13, 1998.

Arthur Andersen & Co.

Chartered Accountants

□ CONSOLIDATED BALANCE SHEETS

	December 31	
	1997	1996
ASSETS		
Current		
Accounts receivable	\$ 31,376	\$ 43,980
Other	4,892	6,221
	36,268	50,201
Property, plant and equipment (Note 2)	548,511	414,504
Total Assets	\$ 584,779	\$ 464,705
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	\$ 51,014	\$ 46,953
Bank loan (Note 3)	169,468	134,880
Site restoration and abandonment	11,785	5,463
Deferred income taxes	78,486	45,432
	259,739	185,775
Shareholders' Equity		
Capital stock (Note 4)	189,493	184,660
Retained earnings	84,533	47,317
	274,026	231,977
Total Liabilities and Shareholders' Equity	\$ 584,779	\$ 464,705

Approved on behalf of the Board:


Director


Director

□ CONSOLIDATED STATEMENTS OF
INCOME AND RETAINED EARNINGS

1997 (except per share amounts)		Year Ended December 31	
	1997		1996
Revenues			
Oil and natural gas	\$ 217,559	\$	173,773
Royalties	(36,102)		(30,870)
Alberta Royalty Credit	1,227		1,469
	182,684		144,372
Expenses			
Operating	48,555		40,975
General and administrative	3,188		2,967
Interest on long-term debt	6,745		9,488
Depletion and depreciation	52,629		42,768
	111,117		96,198
Income before taxes	71,567		48,174
Taxes			
Deferred income taxes (Note 5)	33,054		23,371
Capital taxes	1,297		964
	34,351		24,335
Net income	37,216		23,839
Retained earnings, beginning of year	47,317		23,478
Retained earnings, end of year	\$ 84,533	\$	47,317
Net income per Common Share (Note 6)			
Basic	\$ 0.94	\$	0.66
Fully Diluted	\$ 0.90	\$	0.66

□ CONSOLIDATED STATEMENTS OF
CHANGES IN FINANCIAL POSITION

	Year Ended December 31	
	1997	1996
Operating Activities		
Net income	\$ 37,216	\$ 23,839
Depletion and depreciation	52,629	42,768
Deferred income taxes	33,054	23,371
Unrealized foreign exchange loss	—	73
Cash provided by operating activities	122,899	90,051
Investing Activities		
Additions to property, plant and equipment	(194,118)	(123,495)
Expenditures on abandonments	(928)	(135)
Proceeds on sales of property, plant and equipment	14,732	21,647
Cash used in investing activities	(180,314)	(101,983)
Financing Activities		
Increase (Decrease) in long-term debt	34,588	(24,581)
Issue of common shares	4,833	49,930
Share issue costs	—	(1,999)
Decrease (Increase) in non-cash working capital	17,994	(11,418)
Cash provided by financing activities	57,415	11,932
Increase in cash	—	—
Cash and short-term deposits, beginning of year	—	—
Cash and short-term deposits, end of year	\$ —	\$ —

□ NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1997 and 1996

(all tabular amounts in \$000's, except per share amounts)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Principles of consolidation

The consolidated financial statements include the accounts of Penn West Petroleum Ltd. (the "Company") and its wholly owned subsidiaries and partnership.

b) Other current assets

Other current assets include deposits, prepayments and inventory valued at the lower of cost and net realizable value.

c) Property, plant and equipment

i) Capitalized costs

The full cost method of accounting for oil and natural gas operations is followed whereby all costs of acquiring, exploring and developing oil and natural gas reserves are capitalized. These costs include lease acquisition, geological and geophysical, exploration and development and related overhead costs. Proceeds from the disposition of oil and natural gas properties are accounted for as a reduction of capitalized costs, with no gain or loss recognized unless such disposition results in a significant change in the depletion and depreciation rate.

ii) Depletion and depreciation

Depletion and depreciation of resource properties are calculated using the unit-of-production method based on production volumes before royalties in relation to total proved reserves as estimated by independent engineers. Natural gas volumes are converted to equivalent oil volumes based upon the relative energy content of six thousand cubic feet of natural gas to one barrel of oil. In determining its depletion base, the Company includes estimated future costs to be incurred in developing proven reserves and excludes salvage values and the cost of unevaluated property. Processing facilities, net of salvage, are depreciated based on the estimated useful life of the facilities.

iii) Ceiling test

The carrying amount of property, plant and equipment, net of recorded deferred income taxes and site restoration and abandonment costs, is limited to the sum of estimated future net cash flows from proven reserves and the cost, less impairment, of undeveloped properties. Estimated future capital costs, production-related general and administrative expenses, interest expenses, and applicable income taxes are deducted in determining estimated future net cash flows from proven reserves.

iv) Future site restoration and abandonment costs

A provision has been made for estimated future site restoration and abandonment costs calculated on the unit-of-production method. The 1997 provision of \$7.3 million (1996 - \$3.4 million) is included in depletion and depreciation in the Consolidated Statement of Income.

The calculations in ii) and iii) and iv) are based on sales prices, costs and regulations in effect at the end of the year.

d) Joint ventures

Substantially all of the Company's exploration and development activities are conducted jointly with others and accordingly, the accounts reflect only the Company's proportionate interest in such activities.

e) Hedging activities

The Company uses forward contracts to hedge exposure to commodity price, foreign exchange and interest rate fluctuations. Gains and losses on oil and natural gas and foreign exchange transactions are reported as adjustments to oil and natural gas revenues when the related production is sold and gains or losses on interest rate hedging transactions are reported as adjustments to interest on long-term debt.

f) Foreign currency translation

Amounts denominated in foreign currencies are translated into Canadian dollars at the year end exchange rates. Gains or losses are included in net income, except those related to long-term debt on which the gains or losses are deferred and amortized over the life of the debt.

2. PROPERTY, PLANT AND EQUIPMENT

	December 31	
	1997	1996
Oil and natural gas properties, and production and processing equipment	\$ 737,554	\$ 558,547
Other	3,125	2,746
	740,679	561,293
Accumulated depletion and depreciation	(192,168)	(146,789)
Net book value	\$ 548,511	\$ 414,504

During the year ended December 31, 1997, \$2.4 million (1996 - \$1.8 million) of overhead expenses were capitalized. The cost of unevaluated property excluded from the depletion base as at December 31, 1997, was \$82.6 million (1996 - \$67.5 million).

3. BANK LOAN

	December 31	
	1997	1996
Bankers' acceptances	\$ 169,468	\$ 134,880

The Company has a long-term loan facility arranged with a syndicate of Canadian chartered banks which bears interest at the prime rate and is secured by floating charge debentures covering all assets. The maximum borrowing under the facility is \$270 million comprising a \$200 million production loan facility and a \$70 million operating loan facility. The facility is subject to an annual review by the lenders at which time a lender can request conversion to a term loan with repayment not to exceed 5 years. As at December 31, 1997 the

Company has \$3.7 million of cheques issued in excess of cash on hand, included in accounts payable, which reduced the amount otherwise available to be drawn on the loan facility.

4. CAPITAL STOCK

a) Authorized

- i) Unlimited number of preferred shares issuable in one or more series.
- ii) Unlimited number of voting common shares without nominal or par value.

b) Issued

Common Shares	Number	Consideration
Balance, December 31, 1995	34,831,641	\$ 135,837
Issued for cash	4,000,000	47,000
Issued on exercise of stock options	387,850	2,267
Issued to employee stock savings plan	63,540	663
Share issue expenses, net of deferred income taxes of \$892	-	(1,107)
Balance, December 31, 1996	39,283,031	184,660
Issued on exercise of stock options	675,975	4,079
Issued to employee stock savings plan	45,105	754
Balance, December 31, 1997	40,004,111	\$ 189,493

c) Stock options

Options are issued to employees and directors and are exercisable on a cumulative basis at 20 percent per year for each of the first five years following the year of the grant. Options expire after the end of the fifth year. Changes during the year are summarized as follows:

	Number of Options	Exercise Price	
		From	To
Balance, December 31, 1996	3,442,600	\$2.25	\$12.10
Granted	1,013,000	\$13.90	\$17.60
Exercised	(675,975)	\$2.25	\$11.90
Cancelled	(230,600)	\$2.75	\$16.70
Balance, December 31, 1997	3,549,025	\$2.25	\$17.60

5. INCOME TAXES

The provision for income taxes reflects an effective income tax rate that differs from combined federal and provincial statutory tax rates as follows:

	<i>Years ended December 31</i>	
	1997	1996
Income before taxes	\$ 71,567	\$ 48,174
Corporate income tax rate	44.6%	44.6%
Computed income tax provision	\$ 31,919	\$ 21,486
Increase (Decrease) resulting from:		
Non-deductible Crown payments, net	14,733	11,999
Non-deductible depletion	2,555	2,475
Resource allowance	(15,824)	(12,617)
Other	(329)	28
Deferred income taxes	\$ 33,054	\$ 23,371

6. NET INCOME PER SHARE

Net income per share information is computed by dividing the net income by the weighted average number of common shares outstanding during the year. The fully diluted net income per common share calculations include imputed interest, net of tax, of \$1.6 million (1996 - \$1.3 million) on the potential proceeds from the exercise of stock options.

	<i>Years ended December 31</i>	
	1997	1996
Net income per common share		
Basic	\$ 0.94	\$ 0.66
Fully Diluted	\$ 0.90	\$ 0.66
Weighted average number of common shares outstanding		
Basic	39,791,887	35,879,831
Fully Diluted	43,322,744	39,200,976

7. FINANCIAL INSTRUMENTS

The carrying value of accounts receivable, accounts payable and accrued liabilities and bank loan approximate their fair value.

The Company uses various types of financial instruments to reduce its exposure to fluctuating oil and natural gas prices, foreign exchange rates and interest rates. The Company has the following contract positions outstanding at December 31, 1997:

Exposure	Position Hedged	Pricing	Terms	Market Value of Contract @ Year-end* Gain/(Loss)
Commodities				
Sumas Gas Swap	7,500 MMBTU/D	\$2.16 U.S./MMBTU	November 1, 1997 - March 31, 1998	\$479.6 Cdn.
AECO Gas Swap	10,000 GJ/D	\$1.975 Cdn/GJ	November 1, 1997 - March 31, 1998	\$523.5 Cdn.
AECO Gas Swap	10,000 GJ/D	\$1.65 Cdn/GJ	April 1, 1998 - October 31, 1998	\$617.0 Cdn.
Ventura Gas Swap	5,000 MMBTU/D	\$2.42 U.S./MMBTU	November 1, 1997 - March 31, 1998	\$178.1 Cdn.
WTI Oil	2,000 bbl/D	\$20.25 U.S./bbl	January 1, 1998 - December 31, 1998	\$1,978.9 Cdn.
Foreign Exchange				
U.S. Dollar forward sale	\$1,000 U.S./month	\$1.3468	January 1, 1997 - December 31, 1999	\$(1,737.6) Cdn.
U.S. Dollar forward sale	\$1,000 U.S./month	\$1.3826	January 1, 1997 - December 31, 1999	\$(878.4) Cdn.
U.S. Dollar forward sale	\$1,232 U.S./month	\$1.3668	January 1, 1998 - December 31, 1998	\$(824.9) Cdn.
U.S. Dollar forward sale option	\$1,000 U.S./month	\$1.3826	January 1, 2000 - December 31, 2001	\$(606.0) Cdn.
* based on Canadian dollar of 1.4305 to US dollar				

8. RELATED PARTY TRANSACTIONS

The Company incurred \$78,500 (1996 - \$512,117) for underwriting fees, commissions and consulting services to a firm with directors who are directors of the Company.

□ SUMMARY INFORMATION

Five year summary		Years ended December 31				
	1997	1996	1995	1994	1993	
Financial						
(\$000s, except per share amounts)						
Gross revenues	217,559	173,773	129,068	89,538	20,123	
Cash flow	122,899	90,051	62,989	41,483	9,445	
Basic per share*	3.09	2.51	1.96	1.64	0.56	
Fully diluted per share*	3.01	2.43	1.90	1.51	0.56	
Net income	37,216	23,839	11,957	7,123	4,398	
Basic per share*	0.94	0.66	0.37	0.28	0.26	
Fully diluted per share*	0.90	0.66	0.37	0.28	0.26	
Capital expenditures, net	179,386	101,848	131,938	216,714	39,902	
Total assets	584,779	464,705	379,919	300,721	65,994	
Long-term debt	169,468	134,880	159,388	126,021	24,800	
Shareholders' equity	274,026	231,977	159,315	123,064	32,285	
Common shares outstanding (000s)*:						
Basic	40,004	39,283	34,831	30,312	17,876	
Fully diluted	43,553	42,726	38,138	33,453	19,443	
Market value per common share -High*	20.20	14.50	7.125	9.25	10.65	
(\$/share)						
- Low*	13.35	6.75	4.85	4.50	2.60	
- Close*	15.45	14.00	6.875	5.875	5.00	
Operating						
Production						
Oil and liquids production (bbls/day)	12,604	11,483	10,577	6,934	1,753	
Oil and liquids price (\$/bbl)	21.71	21.80	19.86	19.27	18.39	
Natural gas production (mmcf/day)	164.8	129.0	97.4	58.2	13.0	
Natural gas price (\$/mcf)	1.96	1.74	1.47	1.91	1.72	
Reserves (proven and probable)						
Oil and liquids (mmbbls)	47.7	40.4	33.6	30.5	9.6	
Natural gas (bcf)	628.4	515.0	481.5	328.7	108.6	
Wells drilled (gross)						
Oil	69	63	16	9	5	
Natural gas	71	42	42	39	5	
Dry	22	16	8	9	4	
	162	121	66	57	14	
Undeveloped land holdings, western Canada						
(000s of acres)						
Gross	1,836	1,535	1,571	1027	388	
Net	1,563	1,318	1,206	831	197	
Average working interest (%)	84	86	77	81	51	

* Per share amounts have been adjusted to reflect the consolidation of common shares on a five-for-one basis that occurred in June 1993.

□ QUARTERLY FINANCIAL SUMMARY

	1997				1996			
Three months ended	Mar 31	Jun 30	Sept 30	Dec 31	Mar 31	Jun 30	Sept 30	Dec 31
Financial								
(\$000s, except per share amounts)								
Gross revenues	56,340	47,476	52,647	61,096	38,325	39,684	43,193	52,571
Cash flow	32,351	25,741	28,071	36,736	19,004	19,035	22,123	29,889
Basic per share	0.82	0.65	0.70	0.92	0.54	0.55	0.63	0.79
Fully diluted per share	0.81	0.63	0.68	0.89	0.52	0.53	0.61	0.77
Net income	11,532	7,129	7,820	10,735	4,270	3,661	5,601	10,307
Basic per share	0.29	0.18	0.20	0.27	0.12	0.11	0.16	0.27
Fully diluted per share	0.27	0.18	0.18	0.27	0.12	0.11	0.16	0.27
Operating								
Oil and liquids production (bbls/day)	12,016	12,342	12,890	13,152	11,235	11,305	11,703	11,683
Oil and liquids price (\$/bbl)	24.23	21.01	21.30	20.50	19.38	20.69	22.41	24.63
Natural gas production (mmcf/day)	146.9	165.0	173.0	173.9	119.0	129.9	133.2	134.0
Natural gas price (\$/mcf)	2.28	1.59	1.72	2.27	1.71	1.56	1.55	2.12

Conversions of Units

Imperial	Metric
1 ton	.907 tonnes
1.102 tons	1 tonne
1 acre	.40 hectares
2.5 acres	1 hectare
1 bbl	.159 cubic metres
6.29 bbls	1 cubic metre
1 mcf	28.2 cubic metres
.035 mcf	1 cubic metre
1 mile	1.61 kilometres
.62 miles	1 kilometre

Unless otherwise stated, all financial sums are stated in Canadian dollars.

Abbreviations

bbl	barrel (oil)
mmbbls	million barrels
bbls/day	barrels per day
boe	barrels of oil equivalent
mmboe	million barrels of oil equivalent
mmbtu	million British Thermal Units
mcf	thousand cubic feet (natural gas)
mmcf	million cubic feet
mmcf/day	million cubic feet per day
bcf	billion cubic feet
API	American Petroleum Institute
TSE	The Toronto Stock Exchange
NYMEX	New York Mercantile Exchange
AEUB	Alberta Energy and Utilities Board
WTI	West Texas Intermediate (benchmark crude for pricing)
TCGSL	TransCanada Gas Services Limited (benchmark intra-Alberta gas for pricing)

□ OUR EMPLOYEES

NANCY AMES	CLAYTON GATES	WILLIAM LEWINGTON	DON RAE
WILLIAM ANDREW	LANCE GIBSON	KAREN LIDGREN	AL RALSTON
LES BAILEY	SHELLEY GINTHER	ELIZABETH LOMHEIM	BRIAN REED
MARJORIE BAKER	JENNIFER GOAT	VINCENT LONG	JAMES ROWAN
LEONA BALLMAN	TRACY GODDARD	CAROL LUPYCZUK	GARNET ROYSUM
STEPHEN BATCH	WALLY GRAB	BARRY LYONS	WAYNE RUPTASH
KELLY BATTEN	LEONARD GRANSON	DENNIS MACIBORSKY	KATHY RURAK
DAVE BROOKS	TREVOR GROVER	KEVIN MACINNES	ROBERT SAWYER
WAYNE BRZUS	BEN HALUSZKA	TONY MARCHAND	MAUREEN SCHRADER
RONALD CAWSTON	BRAD HANCOCK	KIM MATERI	IRLANDA SCHWAB
KUN CHEANG	MARK HARDMAN	MATT MAZURYK	CARL SHANTZ
BARRY CHYKERDA	MURIEL HARKNESS	JUNE MCBRIDE	ENETA SHARMA
BRYAN CLAKE	TERRY HAUG	STEVEN MCDONALD	MARK SMITH
BARRY CLARKSON	TREVOR HEIN	WAYNE MCEACHERN	SUSAN SMYTHE
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ROBERT COLLINGS	BOYD HEYLAND	CLARKE MCLEAN	DENNIS STRINGER
TIM CONNOLLY	LAWRENCE HLUSHAK	ALVIN MILLER	DENNIS STUART
TOM COOKSON	NINA HO	DALE MILLER	JOY STUCKLE
DONALD COSMAN	GREGORY HODGSON	ROBERT MISCHUK	GEORGE SWERDAN
DON COTE	ANGELA INGLES	BILL MOODY	TODD TAKEYASU
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VINCENT EKVALL	MICHAEL KLUCZNY	DARRELL OSINCHUK	BRIAN WADDELL
GERRY ELMS	DAN KOCH	RHYS OVERMAN	FRANK WALCER
IZUMI EPP	ISKA KOLACKOVSKY	WILLIAM PARK	BARRY WARNICK
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MERVIN FIRKUS	MAGNI LAKE	GLEN PETRIE	GUY WILSON
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□ CORPORATE INFORMATION

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West Vancouver, B.C.

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Calgary, Alberta

Denis L. Russell
West Vancouver, B.C.

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Chairman

William E. Andrew
President

Larry M. Jones
Vice President, Land &
Corporate Development

Donald J. Rae
Vice President, Exploration

Gerry J. Elms
Treasurer and Secretary

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